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No. 87-792

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

EDEN SERVICES, FRED J. EDEN, JR., AND J. ERIK EDEN,

Petitioners,

v.

RYKO MANUFACTURING CO.,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF OF MARYLAND, NEW JERSEY, PENNSYLVANIA, AND TEXAS AS AMICI CURIAE IN SUPPORT OF PETITIONERS

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The Daily Record Co., Baltimore, MD 21202

EDITOR'S NOTE

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On Petition For A Writ Of
Certiorari To The
United States Court Of Appeals
For The Eighth Circuit

BRIEF OF MARYLAND, NEW JERSEY, PENNSYLVANIA, AND TEXAS AS AMICI CURIAE IN SUPPORT OF PETITIONERS

INTRODUCTION

Maryland, New Jersey, Pennsylvania, and Texas (hereinafter the "Amici States") submit this brief in support of the Petition for a Writ of Certiorari.

INTEREST OF THE AMICI STATES

The Attorneys General of the Amici States are charged by law with the duty to enforce their states' antitrust laws, as well as the federal antitrust laws. In addition, they represent their states and political subdivisions in treble damage actions under the federal antitrust laws, and are authorized by law to bring such actions as parens patriae on behalf of the natural citizens of their states.[1/]

The Amici States, in their capacity as parens patriae, play a major role in federal antitrust enforcement. Moreover, the states' own antitrust laws are generally construed in accordance with federal court decisions interpreting corresponding provisions of the federal laws.[2/] Therefore, the Amici States

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1/ 15 U.S.C. § 15c.

2/ See, e.g., Marin County Bd. of Realtors v. Palsson, 130 Cal. Rptr. 1, 549 P.2d 833 (1976); People v. North Avenue Furniture & Appliance, Inc., 645 P.2d 1291 (Colo. 1982); Neyens v. Roth, 326 N.W.2d 294 (Iowa 1982); Pittsburgh Plate Glass Co. v. Paine & Nixon Co., 182 Minn. 159, 234 N.W. 453 (1931); State v. (Continued)

have a substantial interest in ensuring that federal courts apply the antitrust laws consistently with underlying Congressional policy and with this Court's past decisions.

The Amici States support the contention of Petitioners Eden Services, Fred J. Eden, Jr., and J. Erik Eden ("Eden"), that an illegal price fixing agreement exists when a manufacturer sets distributor's resale prices, but disclaims the existence of any agency relationship in its distributorship contract and places risks of loss on the distributor. Defining the relationship as principal and agent to permit price fixing, as the Eighth Circuit did, severely undercuts the per se rule against vertical price fixing. Petitioners' contention, in contrast, promotes

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Readers Digest Assoc., Inc., 81 Wash.2d 259, 501 P.2d 290 (1972) appeal dismissed, 41 U.S. 945 (1973); Grams v. Boss, 97 Wis.2d 332, 294 N.W.2d 473 (1980). See also, FLA. STAT. § 542.32 (1985); MD. COM. LAW CODE ANN. § 11-202(a)(2) (1983 Repl. Vol.); VA. CODE § 59.1-9.17 (1987).

sound antitrust policy and effective enforcement of the antitrust laws.

SUMMARY OF ARGUMENT

A resale price maintenance ("RPM") agreement between a manufacturer and an independent distributor is illegal per se. In Simpson v. Union Oil Co., 377 U.S. 13 (1964), this Court reinforced the RPM ban. Simpson prevents parties from circumventing the per se rule by merely characterizing their relationship as principal and agent.

The Eighth Circuit's Opinion in Ryko Manufacturing Co. v. Eden Services, 823 F.2d 1215 (8th Cir. 1987) petition for cert. filed, 56 U.S.L.W. 3385 (U.S. Nov. 16, 1987) (No. 87-792), conflicts with both the holding and the spirit of Simpson. By erroneously characterizing the parties' relationship as principal and agent rather than as manufacturer and independent distributor, Ryko reopens the loophole in the per se rule closed by Simpson.

In addition, other circuit courts, while purporting to follow Simpson, have applied conflicting criteria to determine whether a manufacturer and a distributor are legally capable of concerted action necessary to violate section 1 of the Sherman Act, 15 U.S.C. § 1. The confusion caused by these decisions has severely curtailed the Simpson rule and undermined the ban on RPM agreements.

The Amici States are concerned that this erosion of the per se rule against resale price maintenance will have far ranging effects. In certain manufacturer/ distributor settings, vertical price fixing may become essentially per se legal. The Attorneys General will encounter difficulty in enforcing the antitrust laws to protect consumers and foster competition. This Court should, therefore, grant the Petition for a Writ of Certiorari to reaffirm Simpson.

ARGUMENT

I.

RYKO IRRECONCILABLY CONFLICTS WITH SIMPSON AND THEREBY UNDERMINES THE PER SE RULE AGAINST RESALE PRICE MAINTENANCE.

A price fixing agreement between a manufacturer and an independent distributor is per se illegal. Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911). Since Dr. Miles, this Court has consistently applied the per se rule to vertical price fixing. See, e.g., 324 Liquor Corp. v. Duffy, 107 S. Ct. 720 (1987); Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984); Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977); United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944); Federal Trade Commission v. Beech-Nut Packing Co., 257 U.S. 441 (1922).

An exception to the RPM ban exists when a principal sets prices for its agent because the parties to an agency relationship are legally incapable of conspiring for purposes of section 1 of the Sherman

Act, 15 U.S.C. § 1. United States v. General Electric Co., 272 U.S. 476 (1926). Parties cannot, however, engage in resale price maintenance by merely characterizing themselves as principal and agent. In Simpson v. Union Oil Co., 377 U.S. 13 (1964), this Court forcibly closed that loophole in the RPM ban.3/

Simpson holds that resale price maintenance, achieved through a purported agency relationship, is illegal when an examination of the economic realities of the relationship, mainly the allocation of the risks of loss, show the so-called agent to be an independent entrepreneur. Id. at 20-22. This Court found that the retail dealer in Simpson had most of the "indicia of entrepreneurs" and therefore was an "independent businessman" who could agree to fix prices in violation

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3/ In Copperweld Corp. v. Independent Tube Corp., 467 U.S. 752 (1984), this court held that a corporate parent and its wholly owned subsidiary are incapable of violating Section 1 of the Sherman Act because they possess a "complete unity of interest." Id. at 771. This Court explicitly limited its decision to activity of a parent and subsidiary. Copperweld cannot be expanded to apply to agency relationships.

of the Sherman Act. Id. at 20. As a result, this Court ruled that the oil company, which set prices through a consignment arrangement, engaged in illegal price fixing.

Ryko Manufacturing Co. v. Eden Services, 823 F.2d 1215 (8th Cir. 1987), petition for cert. filed, 56 U.S.L.W. 3385 (U.S. Nov. 16, 1987) (No. 87-792), directly conflicts with Simpson and reopens the loophole it closed. Although in Ryko the Eighth Circuit purported to follow Simpson, it recast the relationship between Ryko, a car wash manufacturer, and Eden, an independent distributor, as principal and agent. Thus, the court failed to find concerted action necessary for a violation of the Sherman Act.

Ryko cannot be reconciled with either the spirit or the holding of Simpson. First, the two decisions promote far different policies. Simpson implements the policy that the antitrust laws should be construed broadly to give maximum effect to their underlying purposes. Exemptions should be interpreted narrowly.

See, e.g., Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205, 231 (1979); Goldfarb v. Virginia State Bar, 421 U.S. 773, 787 (1975); U.S. v. McKesson & Robbins, Inc., 351 U.S. 305, 316 (1956). Consequently, the Simpson Court refused to create a consignment exemption to the RPM ban. By ensuring price competition in the marketplace, the Simpson rule benefits consumers.

The Ryko court, on the other hand, applied the antitrust laws narrowly and created a broad exemption by finding an agency relationship between Ryko and Eden. Indeed, the court indicated that price fixing in the Ryko circumstances "would be consistent with sound antitrust policy." 823 F.2d at 1222. Thus, the result in Ryko was inevitably inconsistent with Simpson.

Second, the analysis performed in Simpson was necessary only because the parties had described themselves as principal and agent to avoid the antitrust laws. 377 U.S. at 18-19. Here, however, the

agreement between Ryko and Eden, drafted by Ryko, specifically disclaims an agency relationship.[4/] This provision is a strong indication that the parties intended to remain independent.

Third, a comparison of the economic realities in Ryko with those in Simpson demonstrates Eden was an independent entrepreneur. In Simpson, as the retail price of gasoline dropped, the dealer's commission declined. Likewise, Eden's return on price-fixed National Account Program ("NAP") sales varied with market conditions. Eden's "commission" on NAP sales was the difference between Eden's wholesale cost for the machines and the fixed NAP price. If NAP prices

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4/ The Exclusive Distributorship contract between Eden and Ryko, Pet. App. D at 67a-68a provides:

> It is agreed that this agreement does not constitute the Distributor, the agent or legal representative of the Company for any purposes whatsoever. Distributor is not claiming any right or authority to assume or create any obligation or responsibility, expressed or implied, on behalf of the name of the Company of [sic] to bind Company in any manner or thing whatsoever.

dropped, Eden incurred all of the loss. 823 F.2d at 1220. Ryko bore no risk; it was paid the same amount whether the machine was sold to Eden or to a NAP customer.

The Simpson dealer also bore the risk of loss of the product following delivery, except for acts of God. 337 U.S. at 20. Similarly, Eden bore all risks of loss on sight draft transactions.[5/] On purchase order transactions, the parties shared the loss. Ryko bore the cost of its machinery, but Eden bore the loss of

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[5/] In sight draft transactions, Ryko shipped machinery to Eden who then paid for the machine through a sight draft transfer. Title and risk of loss passed to Eden. To protect itself from the risk of non-payment by the purchaser, Eden required the purchaser to pay in advance. Because the purchaser had already paid, Eden immediately passed title to the purchaser. 823 F.2d at 1219-20, 1227. Based upon Eden's requirement of advance payment, the Eighth Circuit found insufficient shifting of risk of loss to Eden. 823 F.2d at 1227. That conclusion is incorrect. The particular financing arrangement between Eden and the purchaser has no impact upon the transfer of risk of loss between Ryko and Eden, the pertinent risk for the Simpson analysis.

installation.[6/] On all transactions Eden sustained the risk of damage in transit, 823 F.2d at 1225 n.4, a risk not borne by the Simpson dealer.

In sum, Eden was more independent from Ryko than the Simpson dealer was from Union Oil. Thus, the Eighth Circuit's finding that Eden was Ryko's agent directly contravenes Simpson and Simpson's reinforcement of the per se rule.

[6/] In its analysis, the Eighth Circuit looked only at the car wash machine itself. Yet, the customer bought a fully installed, operating car wash. This included both a good (the car wash machine manufactured by Ryko) and a service (installation by Eden). Ryko fixed the price for both the good and the service on NAP sales. Ryko received its usual wholesale price (the same price it received on all purchases involving distributors) and Eden received the difference between the NAP price and the wholesale price. From this amount, Eden had to recoup all of its sales costs plus all of its costs of installation, including shipping damage repair costs. 823 F.2d at 1218-28. Even under the Eighth Circuit's narrow reading of Simpson, Eden must have been an independent businessman for the service component for which it bore all economic risks.

II.

THE COURT SHOULD RESOLVE CONFLICTING APPLICATIONS OF SIMPSON BY THE COURTS OF APPEAL.

While the Eighth Circuit approach in Ryko misapplies Simpson, the rule established by the Seventh Circuit disregards Simpson. In Morrison v. Murray Biscuit Co., 797 F.2d 1430, 1436 (7th Cir. 1986), the Seventh Circuit, although citing Simpson, formulated its own rule that if an "agency relationship has a function other than to circumvent the rule against price fixing," the principal and agent become a single entity incapable of concerted action. Accord Illinois Corporate Travel v. American Airlines, Inc., 806 F.2d 722, 724-26 (7th Cir. 1986). No matter how strong the Simpson "indicia of entrepreneurs," Morrison would find no concerted action if the agency had a function other than price fixing.

In Simpson, Union Oil and its dealer were found to have conspired even though the consignment scheme

had at least one function other than price fixing: it minimized the dealer's investment in his inventory of gasoline.[7/] Under the Seventh Circuit's rule, however, Union Oil and Simpson would be legally incapable of concerted action. Thus, the Morrison rule cannot be reconciled with Simpson's holding.

The Seventh Circuit's rule is an unwarranted departure from the per se rule against resale price maintenance in manufacturer/distributor arrangements. Any manufacturer desiring to fix retail prices could create an "agency" with at least one function other than price fixing.[8/]

[7/] Additional functions for the consignment scheme might also be postulated. For instance, in Parrish v. Cox, 586 F.2d 9, 12 (6th Cir. 1978), the Court found that the consignment arrangement maintained quality.

[8/] Perhaps Morrison can be explained by the Seventh Circuit's antipathy to the per se rule against resale price maintenance. The Seventh Circuit still found the rationale of the per se rule "unclear," despite recognizing that, following Continental T.V. Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), the Supreme Court had reaffirmed the per se rule, California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc., 445 U.S. 97, 102-03 (1980). Morrison, 797 F.2d at 1438. (Continued)

The Seventh Circuit's position is the most extreme attempt among the circuits to circumvent Simpson, but other courts have also interpreted Simpson narrowly, and have thereby limited the scope of the antitrust laws. See e.g., Hardwick v. Nu-Way Oil Co. Inc., 589 F.2d 806, 809-10 (5th Cir.), cert. denied 444 U.S. 836 (1979); Mesirow v. Pepperidge Farm, Inc., 703 F.2d 339, 341-43 (9th Cir. 1983), cert. denied 464 U.S. 820 (1983); Pogue v. International Industries, Inc., 524 F.2d 342 (6th Cir. 1975).

Not all circuit court decisions misapply Simpson. For example, Call Carl, Inc. v. BP Oil Corp., 554 F.2d 623, 627-28 (4th Cir.) cert. denied 434 U.S. 923 (1977); Greene v. General Foods Corp., 517 F.2d

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Unable to attack the rule directly, the court was inclined to create a broad exception to its application. See Isaksen v. Vermont Castings, Inc., 825 F.2d 1158, 1161-62 (7th Cir. 1987) petitions for cert. filed, 56 U.S.L.W. 3322 (U.S. Oct. 14, 1987) (No. 87-610), 56 U.S.L.W. 3356 (U.S. Nov. 2, 1987) (No. 87-728).

635, 651-58 (5th Cir. 1975) cert. denied 424 U.S. 942 (1976), and Atlantic Refining Co. v. Federal Trade Commission, 344 F.2d 599 (6th Cir. 1965), follow both the rule and the spirit of Simpson. Because Ryko conflicts with Simpson, it also conflicts with those circuit court decisions following Simpson. Thus, this Court should grant the Petition to resolve the conflict among the circuits.

III.

THE RYKO DECISION HAS POTENTIALLY DETRIMENTAL EFFECTS ON ANTITRUST ENFORCEMENT.

Ryko, like Morrison, emasculates Simpson and has potentially far-reaching effects on antitrust enforcement. Many manufacturers could characterize their arrangements with distributors as an agency for antitrust purposes under Ryko, or as serving a function other than price fixing under Morrison. For example, merely by requiring purchase orders to be in the manufacturer's name rather than the distributor's

name and by shipping directly to the purchaser, the manufacturer would likely satisfy the Ryko criteria and could fix prices with impunity. The same manufacturer would satisfy the Morrison test by establishing some function other than resale price maintenance, for example quality control. See supra note 7.

Vertical price fixing would become "lawful per se" in divers situations, see Illinois Corporate Travel, 806 F.2d at 729, a result which would severely hamper the Attorneys General in prosecuting resale price maintenance cases. Only in the most egregious cases could a jury be convinced that no "agency" existed for antitrust purposes.

In light of the uncertainty caused by the conflicting court decisions, this Court should reaffirm Simpson. The basic reasoning of Simpson remains sound. The courts should still examine, case by case, whether distributors possess the "indicia of

entrepreneurs." 377 U.S. at 20. If so, the manufacturer and distributor are capable of concerted action in restraint of trade. This Court should clarify and expand the Simpson indicia, however, to ensure the vitality of the per se rule.[9/]

Unless this Court corrects decisions like Ryko and Morrison, manufacturers will continue to circumvent the per se rule against price fixing simply by restructuring their transactions. This Court should not now condone a major exception to its long-held rule that vertical price fixing is per se illegal. This Court should grant the Petition for a Writ of Certiorari.

9/ Moreover, this significant shift away from the per se rule against price fixing is occurring without any action by Congress. Although the courts originally formed the per se rule, the rule has become entrenched in the law. Any diminution of the rule should, therefore, come from Congress.

IV.

CONCLUSION

For the foregoing reasons, this Court should grant the Petition and review the first question presented by Petitioners.

DATED: December 15, 1987

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